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UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

In re)	No. 08-12206 AJ
)	
LOHREY ENTERPRISES, INC.,)	Chapter 7
)	<u>EXPEDITED HEARING REQUESTED</u>
)	
)	

**UNITED STATES TRUSTEE'S MEMORANDUM
OF POINTS AND AUTHORITIES IN SUPPORT OF
MOTION TO REMOVE TRUSTEE RICHARD SCHWALBE
AND TO FREEZE ESTATE BANK ACCOUNTS**

Sara L. Kistler, the Acting United States Trustee for Region 17 ("U.S. Trustee"), submits this memorandum in support of her motion under 11 U.S.C. § 324(a) for entry of an order removing Richard Schwalbe as trustee for cause pursuant to 11 U.S.C. § 324(a) on the grounds that Mr. Schwalbe is unavailable to act as trustee and recent criminal charges and incarceration place undue risk on this estate. In addition, the UST requests that the estate bank accounts be frozen to maintain the status quo and further that the UST be given access to all estate account records to seek to account for the funds of the estate.

FACTUAL STATEMENT

Mr. Schwalbe was arrested on January 26, 2010, based on a felony complaint alleging, *inter alia*, the theft and embezzlement of \$1.37 million from a Silicon Valley company. He is being held without bail. Neither trustee's counsel Patricia Lyon nor Mr. Schwalbe's proposed criminal counsel knew when or if they will be in contact with the trustee.

1 ARGUMENT

2 11 U.S.C. § 324(a) provides that “[T]he court, after notice and a hearing, may remove a trustee,
3 other than the United States Trustee, or an examiner, for cause.” Cause is not defined in the Bankruptcy
4 Code and is left for the courts to determine on a case by case basis. *In re AFI Holdings Inc.*, 355 B.R.
5 139, 155 (9th Cir.BAP 2006), *aff’d*, 530 F.3d 832 (9th Cir. 2008). A trustee may be properly removed for
6 failure to perform trustee duties. *In re AFI Holdings Inc.*, Id. at 148, and for delay in case
7 administration. *In re Island Amusements Inc.*, 74 B.R. 14 (Bankr.D.P.R. 1987). Courts have also found
8 that removal is warranted where there is an appearance of impropriety. *In re AFI Holdings Inc.*, 355
9 B.R. at 155 (9th Cir.BAP 2006), *aff’d*, 530 F.3d 832 (9th Cir. 2008) (lack of disinterest creates an
10 appearance of impropriety).

11 In this case, the trustee’s immediate and potentially longer term unavailability warrants removal.
12 Given the sensitive juncture of the case with a sale pending, the UST submits that is unclear whether the
13 trustee will be out of jail to do his work. Even if he is free on bail, his focus will be elsewhere.

14 The trustee’s arrest for embezzlement and theft create an appearance of impropriety. Millions of
15 dollars in estate asset should not be trusted to one with pending criminal allegations involving
16 embezzlement and theft of \$1.37 million lest the creditors and the public lose confidence in the
17 bankruptcy system.

18 CONCLUSION

19 Based on the foregoing, the UST submit this court should remove Richard Schwalbe as trustee.
20 Additionally, the Court should order that all estate accounts be frozen to maintain the status quo and that
21 the UST be given full access to all account records to fully account for estate funds.

22 Dated: January 28, 2010

Respectfully submitted,

23 Sara L. Kistler,
24 Acting United States Trustee

25 By: /s/Patricia A. Cutler (#50352)
Attorney for the U.S. Trustee